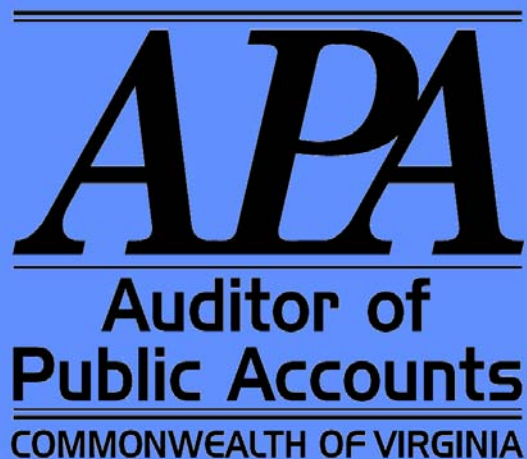


**DEPARTMENT OF
PROFESSIONAL AND OCCUPATIONAL REGULATION**

**REPORT ON AUDIT
FOR THE YEARS ENDED
JUNE 30, 2008 AND JUNE 30, 2009**



AUDIT SUMMARY

Our audit of the Department of Professional and Occupational Regulation (Department) for the years ended June 30, 2008, and June 30, 2009 found:

- proper recording and reporting of all transactions, in all material respects, in the Commonwealth Accounting and Reporting System and the Department's internal systems;
- a matter involving internal control and its operations necessary to bring to management's attention; and
- no instances of noncompliance with applicable laws and regulations or other matters that are required to be reported.

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AUDIT FINDINGS AND RECOMMENDATIONS

Complete a Detailed Risk Assessment for All Agency Systems

The Department of Professional and Occupational Regulation (Department) does not have an adequate Risk Assessment completed for all agency systems. In our review, we determined the following:

- The Risk Assessment for the Enforcement Tracking System (ETS) did not include the identification of vulnerabilities, threats, and risk. Also the risk likelihood ratings, risk impact analysis, and overall risk ratings were not complete for ETS.
- The Risk Assessments for ETS and the Commerce Licensing and Enforcement Systems (CLES) identified both systems as non-essential even though they support critical functions of the Department.
- The Department has not completed a Risk Assessment for the new EAGLES licensing and enforcement system and has already started implementation of the system.

The Commonwealth's information security standards require that agencies prepare Risk Assessments for all agency owned systems. A detailed Risk Assessment is necessary to identify potential threats to an IT system and the environment in which it operates. The Risk Assessment should determine the likelihood that threats will materialize and identify and evaluate the vulnerabilities.

We recommend that the Department reevaluate all agency systems and determine if they support critical functions or contain sensitive data. Based on this evaluation, the Department should update or complete Risk Assessments for each system.

AGENCY HIGHLIGHTS

The Department of Professional and Occupational Regulation (Department) protects the citizens of the Commonwealth by regulating commercial occupations and certain professions as designated by the General Assembly. The Department's responsibilities include certification, licensing, investigation, compliance monitoring, fee collection, record maintenance, and enforcement. The Department provides centralized administrative, examination, and enforcement functions to the following boards:

APELSCIDLA*	Geology
Asbestos, Lead, and Home Inspectors	Hearing Aid Specialists
Auctioneers	Opticians
Barbers and Cosmetology	Polygraph Examiners
Boxing and Wrestling	Real Estate
Branch Pilots	Real Estate Appraisers
Cemeteries	Soil Scientists and Wetland Delineators
Common Interest Community Management	Waste Management Facility Operators
Contractors	Waterworks and Wastewater Works Operators
Fair Housing	

*Architects, Professional Engineers, Land Surveyors, Certified Interior Designers, and certified Landscape Architects

Changes to the board structure during the audit period include the creation of the Common Interest Community Managers Board on July 1, 2008, previously part of the Real Estate Board. The Board was established to regulate Common Interest Community Managers and their supervisory and managerial employees.

Systems Development Project

The Department is implementing a new licensing and enforcement system called EAGLES that will expand public access through online licensing and permitting services, and will also eliminate the maintenance costs associated with their current system. The Department began project execution on EAGLES in October 2007 with an initial project cost estimate of approximately \$2.9 million. The project schedule is broken down into three separate releases. The first release was on schedule and went live in September 2009.

Even with the successful completion of the first release, the overall EAGLES project has slipped behind schedule, primarily due to the project team underestimating the complexity and length of time required to customize and implement the system. The Department must customize the out-of-the-box software for each board to allow for the individual statutory requirements. These customizations require extensive work by the vendor as well as extensive testing by the Department to ensure functionality in the production environment. Also, the Department underestimated the extent of resources needed to fulfill operational as well as project responsibilities. Staff are currently splitting time between these responsibilities, which has led to additional schedule slippage.

Representatives from the Auditor of Public Accounts as well as the Virginia Information Technologies Agency Project Management Division (VITA PMD) met with the Department in July 2009 to address concerns with the project. The Auditors and VITA PMD discussed the initial estimates for the re-baselining, moving the project closeout date to 2013, and the need to increase the project budget. The revised re-baseline costs are approximately \$5.35 million, and the new target for the project extends until 2014 for the remaining two releases.

The project team is currently working on completing the first release and preparing documentation for the final two releases. We will continue to monitor the project throughout its implementation and work with VITA PMD to consider alternatives and recommendations.

FINANCIAL INFORMATION

The Commonwealth Accounting and Reporting System includes all financial data except for the activity of three recovery funds. The Department records licensing fees and the expenses associated with regulation in its special revenue funds. The Department records the collection of monetary penalties in the state Literary Fund.

The schedule below compares the Department's budgeted versus actual expenses for fiscal years 2009 and 2008. The Department received and retained approximately \$20.1 million in fiscal year 2009 and \$19.5 million in fiscal year 2008 for operating budget expenses. During fiscal year 2008, the Department increased its budget by a carry forward of unexpended funds from the previous fiscal year that the Department used during 2008 to cover moving expenses associated with the office relocation. Additionally, the Department's annualized salary costs for 32 new positions, the creation of the Common Interest Community Management Board and continuing health premium increases, accounts for the increase between the 2008 and 2009 original budget amounts.

Analysis of Budgeted and Actual Expenses Fiscal Years Ended June 30, 2009 and June 30, 2008

Fiscal year:	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual Expenses</u>
2009	\$19,558,546	\$20,079,983	\$18,224,159
2008	\$17,301,875	\$19,481,262	\$18,146,909

The Department allocates administrative expenses, legal costs, and information system costs to the various boards using a cost allocation system. The Department's actual expenses were less than budget in both fiscal years 2008 and 2009. The Department's payroll expenses of \$11,894,617 in fiscal year 2008 and \$13,139,541 in fiscal year 2009 accounted for 66 percent and 72 percent, respectively, of total expenses. The increase in payroll is a result of over 30 new employees hired during fiscal year 2009 to aid in the investigation and resolution of complaints brought to the regulatory boards. The majority of the remaining expenses are contractual services which mainly consist of VITA services and cost incurred for the EAGLES project. During fiscal years 2008 and 2009, the Department also collected and deposited penalties from sanctions into the Commonwealth's Literary Fund of \$394,864 and \$509,528, respectively.

Board Activity

The Department uses special revenue funds to account for the daily operations. The Code of Virginia requires separate special revenue funds for the activities of the Boxing & Wrestling Board and the Common Interest Community Management Board. The Department records its remaining activities in a single dedicated special revenue fund for all the other boards. We have consolidated all of these funds in the schedules presented in this report. The largest source of revenue comes from licensing fees for applications and renewals.

The following schedule summarizes the activity of the Department's operating funds for fiscal years 2008 and 2009.

Summary of Operating Activity

	<u>2008</u>	<u>2009</u>
Revenues	\$16,477,256	\$16,928,834
Expenses	<u>17,741,381</u>	<u>17,779,323</u>
Revenues less expenses	(1,264,125)	(850,489)
Net transfers	<u>(70,240)</u>	<u>(13,890)</u>
Change in cash balance	(1,334,365)	(864,379)
Prior year cash balance	<u>17,256,039</u>	<u>15,921,674</u>
Current year cash balance	<u>\$15,921,674</u>	<u>\$15,057,295</u>

Source: Commonwealth Accounting and Reporting System, Funds 0200, 0259 & 0900

The schedule on the following page summarizes the activity and cash balance of the Department's operating funds by Board.

Summary of Operating Activity by Board
Fiscal Years 2008 and 2009

	<u>APELSCIDLA*</u>	<u>Asbestos Lead and Home</u>	<u>Auctioneers</u>	<u>Barbers and Cosmetology</u>	<u>Boxing and Wrestling</u>	<u>Branch Pilots</u>	<u>Cemeteries</u>
2007 Cash balance	<u>\$1,808,096</u>	<u>\$575,742</u>	<u>\$414,609</u>	<u>\$1,487,405</u>	<u>\$193,469</u>	<u>\$21,590</u>	<u>\$235,893</u>
2008 Revenue	<u>1,577,018</u>	<u>192,510</u>	<u>30,865</u>	<u>2,310,707</u>	<u>190,944</u>	<u>7,720</u>	<u>17,275</u>
2008 Expenses	<u>1,480,271</u>	<u>268,178</u>	<u>74,470</u>	<u>2,728,543</u>	<u>171,864</u>	<u>3,816</u>	<u>65,259</u>
2008 Cash balance	<u>1,904,843</u>	<u>500,074</u>	<u>371,004</u>	<u>1,069,569</u>	<u>212,549</u>	<u>25,494</u>	<u>187,909</u>
2009 Revenue	<u>1,559,417</u>	<u>190,366</u>	<u>68,235</u>	<u>2,478,692</u>	<u>214,639</u>	<u>(1,840)</u>	<u>32,535</u>
2009 Expenses	<u>1,431,758</u>	<u>233,419</u>	<u>69,645</u>	<u>2,804,921</u>	<u>196,145</u>	<u>3,873</u>	<u>53,844</u>
2009 Cash balance	<u>\$2,032,502</u>	<u>\$457,021</u>	<u>\$369,594</u>	<u>\$ 743,340</u>	<u>\$231,043</u>	<u>\$19,781</u>	<u>\$166,600</u>
	<u>Common Interest Community</u>	<u>Contractors</u>	<u>Fair Housing</u>	<u>Geology</u>	<u>Hearing Aid Specialists</u>	<u>Opticians</u>	<u>Polygraph Examiners</u>
2007 Cash balance	<u>\$185,310</u>	<u>\$3,572,543</u>	<u>\$ -</u>	<u>\$112,767</u>	<u>\$130,968</u>	<u>\$115,868</u>	<u>(\$ 9,868)</u>
2008 Revenue	<u>172,516</u>	<u>6,743,690</u>	<u>20,675</u>	<u>32,065</u>	<u>13,880</u>	<u>58,490</u>	<u>18,690</u>
2008 Expenses	<u>180,897</u>	<u>7,897,147</u>	<u>20,675</u>	<u>32,852</u>	<u>45,726</u>	<u>91,167</u>	<u>11,732</u>
2008 Cash balance	<u>176,929</u>	<u>2,419,086</u>	<u>-</u>	<u>111,980</u>	<u>99,122</u>	<u>83,191</u>	<u>(2,910)</u>
2009 Revenue	<u>716,877</u>	<u>6,962,106</u>	<u>41,079</u>	<u>2,465</u>	<u>23,610</u>	<u>176,170</u>	<u>17,250</u>
2009 Expenses	<u>355,232</u>	<u>8,018,140</u>	<u>41,079</u>	<u>28,160</u>	<u>51,146</u>	<u>106,306</u>	<u>11,055</u>
2009 Cash balance	<u>\$538,574</u>	<u>\$1,363,052</u>	<u>\$ -</u>	<u>\$ 86,285</u>	<u>\$ 71,586</u>	<u>\$153,055</u>	<u>\$ 3,285</u>

Summary of Operating Activity by Board
Fiscal Years 2008 and 2009 (continued from previous page)

	<u>Real Estate</u>	<u>Real Estate Appraisers</u>	<u>Soil Scientists Wetland Professionals</u>	<u>Waste Mgmt Facility Operators</u>	<u>Waterworks Wastewater Operators</u>	<u>Miscellaneous</u>	<u>Total</u>
2007 Cash balance	<u>\$7,658,980</u>	<u>\$392,006</u>	<u>\$44,771</u>	<u>\$103,514</u>	<u>\$150,275</u>	<u>\$62,101</u>	<u>\$17,256,039</u>
2008 Revenue	4,476,345	329,490	24,873	20,650	238,350	503	\$16,477,256
2008 Expenses	<u>4,195,694</u>	<u>309,518</u>	<u>11,021</u>	<u>27,661</u>	<u>206,360</u>	<u>(11,230)</u>	<u>\$17,811,621</u>
2008 Cash balance	<u>7,939,631</u>	<u>411,978</u>	<u>58,623</u>	<u>96,503</u>	<u>182,265</u>	<u>73,834</u>	<u>\$15,921,674</u>
2009 Revenue	3,969,412	195,094	47,050	23,540	212,135	2	\$16,928,834
2009 Expenses	<u>3,903,713</u>	<u>204,485</u>	<u>11,630</u>	<u>25,425</u>	<u>183,300</u>	<u>59,937</u>	<u>\$17,793,213</u>
2009 Cash balance	<u>\$8,005,330</u>	<u>\$402,587</u>	<u>\$94,043</u>	<u>\$ 94,618</u>	<u>\$211,100</u>	<u>\$13,899</u>	<u>\$15,057,295</u>

*Architects, Professional Engineers, Land Surveyors, Certified Interior Designers, and certified Landscape Architects

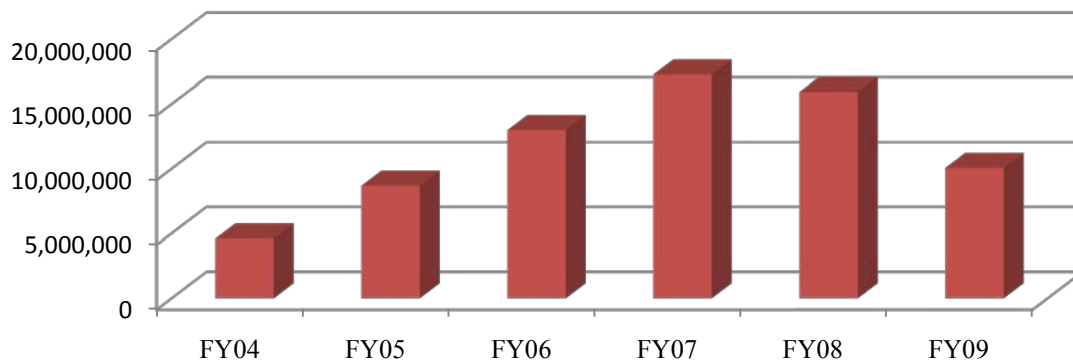
The Miscellaneous column in the previous table represents activity not allocated to a specific board. Of the \$13,899 of unallocated cash at fiscal year end 2009, \$10,000 is a result of a donation to the Asbestos Board in fiscal year 2007 for educational programs. The Board keeps these funds in a separate fund from its normal operations.

Each board is self-supporting through regulant-assessed fees. The Code of Virginia requires the individual boards to adjust fees at the end of each biennium if expenses vary more than ten percent from revenues. Adjusting a fee schedule is a lengthy process that can take up to three years to fully implement. Thus, boards set fees at a level that will support the boards' activity for three to four biennia.

Revenues will generally exceed expenses for the first few years after a fee increase. This allows the boards to establish cash balances, which they use in the later years when expenses begin to exceed revenues. When this occurs, the Department proposes new fee schedules to the boards for approval. The Department continually monitors each board to determine if a fee increase or decrease is necessary, since economic factors greatly impact the activity of each board.

In past years, several boards had accumulated substantial cash balances due to revenues exceeding expenditures in the periods immediately following a fee increase. However, during fiscal years 2008 and 2009, many of the boards experienced increased expenses and received less revenue due to fewer applicants and renewals as a result of economic conditions. This led to an overall decrease in available cash balance for ten of the 19 boards. Currently, three boards are in the process of adjusting fees. The board of Contractors has approved a fee increase expected to take effect in early 2010 pending the Governor's approval. The Barber & Cosmetology board and the board of Hearing Aid Specialists are both currently reviewing proposed fee increases. The Department will continue to evaluate the activity of all boards to ensure fee schedules are appropriate. The following chart summarizes the changes in available cash reserves for the Department for fiscal years 2004 through 2009.

Cash Reserve Balances
Fiscal Years 2004-2009



Recovery Funds

The Department controls three recovery funds held in the Local Government Investment Pool (LGIP), a short-term investment pool managed by the State Treasurer. Fees from the respective boards fund the recovery funds, which pay individuals who have claims against licensees who are bankrupt, cannot be located, or otherwise cannot pay a claim when found guilty of improper and dishonest conduct. The Code of Virginia established the Common Interest Community Management Recovery Fund in fiscal year 2009 with the creation of the Common Interest Community Management Board. The following schedule shows the cash and investment balances for the recovery funds for fiscal years 2008 and 2009.

Cash and Investment Balances
Fiscal Years 2008-2009

	<u>Fiscal Year</u> 2008	<u>Fiscal Year</u> 2009
Virginia Common Interest Community Management Recovery Fund	\$ -	\$ 106,255
Virginia Contractor Transaction Recovery Act Fund	\$2,060,658	\$ 859,670
Virginia Real Estate Transaction Recovery Act Fund	\$3,127,124	\$3,031,935

Due to an increased number of claim payments and a decrease in applicants and renewals in 2008 and 2009, the Contractor Recovery Fund has seen a large decrease in its cash and investment balance. The Code of Virginia allows the Contractor Recovery Fund to assess an additional fee to all regulants to increase the overall cash balance when necessary. In March 2009, the Contractors board assessed each regulant who was up for renewal in 2009 an additional \$20 fee to support the Contractor Recovery Fund.

Fair Housing Assistance Program

The Department's federal fund consists primarily of revenue and expenses from its participation in the Fair Housing Assistance Program administered by the U.S. Department of Housing and Urban Development (HUD). Pursuant to the cooperative agreement between HUD and the Department, HUD provides financial support to assist with the Department's processing of complaints alleging unlawful discrimination in housing. Additionally, HUD provides funds for training of agency staff involved with the processing of these complaints.



Commonwealth of Virginia

Auditor of Public Accounts

P.O. Box 1295

Richmond, Virginia 23218

Walter J. Kucharski, Auditor

October 7, 2009

The Honorable Timothy M. Kaine
Governor of Virginia

The Honorable M. Kirkland Cox
Chairman, Joint Legislative Audit
and Review Commission

We have audited the financial records and operations of the **Department of Professional and Occupational Regulation** for the years ended June 30, 2008, and June 30, 2009. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Audit Objectives

Our audit's primary objectives were to evaluate the accuracy of recorded financial transactions on the Commonwealth Accounting and Reporting System and in the Department's internal systems, review the adequacy of the Department's internal controls, test compliance with applicable laws and regulations and review corrective actions of audit findings from prior year reports.

Audit Scope and Methodology

The Department's management has responsibility for establishing and maintaining internal control and complying with applicable laws and regulations. Internal control is a process designed to provide reasonable, but not absolute, assurance regarding the reliability of financial reporting, effectiveness and efficiency of operations, and compliance with applicable laws and regulations.

We gained an understanding of the overall internal controls, both automated and manual, sufficient to plan the audit. We considered significance and risk in determining the nature and extent of our audit procedures. Our review encompassed controls over the following significant cycles, classes of transactions, and account balances.

Revenues
Payroll Expenses
Contractual Service Expenses

Recovery Fund Accounts
Small Purchase Charge Card
Information Security

We performed audit tests to determine whether the Department's controls were adequate, had been placed in operation, and were being followed. Our audit also included tests of compliance with provisions of applicable laws and regulations. Our audit procedures included inquiries of appropriate personnel, inspection of documents, records, and contracts, and observation of the Department's operations. We tested transactions and performed analytical procedures, including budgetary and trend analyses.

Conclusions

We found that the Department of Professional and Occupational Regulation properly stated, in all material respects, the amounts recorded and reported in the Commonwealth Accounting and Reporting System and in its internal systems. The Department records its financial transactions on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America. The financial information presented in this report came directly from the Commonwealth Accounting and Reporting System.

We noted a certain matter involving internal control that requires management's attention and corrective action. This matter is described in the section entitled "Audit Findings and Recommendations."

The Department has taken adequate corrective action with respect to audit findings reported in the prior year that are not repeated in this letter.

Exit Conference and Report Distribution

We discussed this report with management on October 21, 2009. Management's response has been included at the end of this report.

This report is intended for the information and use of the Governor and General Assembly, management, and the citizens of the Commonwealth of Virginia and is a public record.

AUDITOR OF PUBLIC ACCOUNTS

SLJ:alh



COMMONWEALTH of VIRGINIA
DEPARTMENT OF PROFESSIONAL AND OCCUPATIONAL REGULATION

JAY W. DeBOER
DIRECTOR

October 22, 2009

DEPUTY DIRECTORS:

NICK A. CHRISTNER
Compliance & Investigation

MARK N. COURTNEY
Licensing & Regulation

STEVEN L. ARTHUR
Administration & Finance

Mr. Walter J. Kucharski
Auditor of Public Accounts
Post Office Box 1295
Richmond, VA 23218

Dear Mr. Kucharski:

Thank you for giving us an opportunity to respond to your audit finding on Risk Assessments for Agency Systems. The Department is committed to a strong system of internal control and welcomes this opportunity to improve our systems documentation.

The Enforcement Tracking System and Commerce Licensing and Enforcement System were classified as non-essential in our risk assessment documents due to a misunderstanding over the definition of essential systems. After discussing the issue with your staff we agree that these systems should be designated as mission essential. I have directed my Information Systems Manager to update our Risk Assessment documents for this change, together with the other changes recommended in your audit report.

Sincerely,

Jay W. DeBoer

DEPARTMENT OF PROFESSIONAL AND OCCUPATIONAL REGULATION
as of June 30, 2009

Jay W. DeBoer
Director

Steven L. Arthur
Deputy Director for Administration and Finance